Board of Housing:

The Montana Housing Act of 1975 created the Montana Board of Housing. The Board is an agency of the State and operates within the Department of Commerce for administrative purposes. Under the Housing Act the Board does not receive appropriations from the State's general fund and is completely self-supporting. Substantially all of the funds for the Board's operations and programs are provided by the private sector through the sale of tax-exempt bonds. The powers of the Board are vested in a seven member Board, appointed by the Governor, subject to the confirmation of the State Senate. The Board provides policy direction to the agency staff, authorizes bond issues, approves development financing and evaluates Board Housing Programs. These programs include the Single Family Program, Recycled Single Family Program, Multifamily Loan Programs, Low Income Housing Tax Credit Program, Housing Revolving Loan Fund and the Reverse Annuity Mortgage (RAM) Program.

The Board of Housing is funded by four enterprise funds with revenues derived from an administrative charge applied to projects and mortgages financed. Under the Montana Housing Act of 1975, the board does not receive any general fund, and is completely self-supporting.

Board of Housing Goals & Objectives:

- Continue automation of functions to improve operational efficiency and decrease need for additional staff. Continue to look at new ways of operating to improve efficiency and timeliness.
- Manage the assets of the Board in the most effective manner to enhance the ability to provide housing finance for lower income Montanans. Use any program earnings to recycle into new mortgages or call bonds.
- Continuously review programs to determine if they are meeting the needs of the population they are intended to serve. Continue to change program requirements based on current conditions.
- Increase education and outreach to the citizens of Montana and the Board's customers and servicers through public appearances, workshops, print media, and other means as appropriate.
- Provide training to lenders and Realtors, as well as work with non-profits to provide homebuyer education and post purchase education.
- Develop and implement creative methods of financing multifamily rental housing.
- Review opportunities for preservation of federally financed housing, and work with HUD on restructuring of multifamily properties when appropriate.
- Find ways aimed at lowering the cost of housing including The Plan Book and The Governor's House Program.
- Develop programs that meet the needs of populations that are not currently being served.
- Promote the use of the funds within the Housing Revolving Loan Account (HRLA).
- Use Internet web page to provide updated information to persons interested in Board activities and programs.

Board of Housing HB 576 Program Description:

The Montana Housing Act of 1975 created the Montana Board of Housing. The Board is an agency of the State and operates within the Department of Commerce for administrative purposes. Under the Housing Act the Board does not receive appropriations from the State's general fund and is completely self-supporting. Substantially all of the funds for the Board's operations and programs are provided by the private sector through the sale of tax-exempt bonds. The powers of the Board are vested in a seven member Board, appointed by the

Governor, subject to the confirmation of the State Senate. The Board provides policy direction to the agency staff, authorizes bond issues, approves development financing and evaluates Board Housing Programs. These programs include the Single Family Program, Recycled Single Family Program, Multifamily Loan Programs, Low Income Housing Tax Credit Program, Housing Revolving Loan Fund and the Reverse Annuity Mortgage (RAM) Program.
The Board of Housing is funded by four enterprise funds (accounting entities 06030, 06031, 06078, and 06079) with revenues derived from an administrative charge applied to projects and mortgages financed. There are no direct appropriations provided in HB 2; the Board is completely self-supporting.

The Board of Housing is primarily mandated in Title 2, Chapter 15; and Title 90, Chapter 1, and Chapter 6, MCA.

Customers include households that qualify for the Board's programs to either rent or buy their own home. The Board partners with brokers, Realtors, banks, real estate lenders, builders, developers, contractors, non-profit housing providers and other governmental entities. Working together with its partners, the Board provides programs that allow a household to rent an apartment or house at an affordable rent. It allows a qualifying household to obtain a lower rate mortgage that will allow them to be able to afford a home that meets their household needs. It also allows qualifying senior households the opportunity to access the equity in their homes to help them afford to stay in their house through a reverse mortgage.

There has not been any significant program, service, or customer base change since the last session.

Board of Housing HB 576 Revenues, Expenses, and Fund Equity:

Revenue Description:

Single Family Charges:

According to state statute and, in some cases, the Internal Revenue Code, the Board is allowed to earn the amounts that are presented on the "Report on Internal Service and Enterprise Funds". The Board earns the bulk of its income from the spread between the interest yield on the Single Family Mortgage loans and the yield on the bonds. The Board is allowed to earn 1 1/2% on Pre 1980 Single Family Programs and 1 1/8% on the Post 1980 Single Family Programs.

Financial institutions that originate Single Family loans for the Board may charge two points, which they keep or originate loans with no points, at a slightly higher rate and have the loans purchased at 102%. Approximately 1% of the loans have 2 points charged. According to tax law, origination points must be included in the amount that the Board can earn. Operating expenses and servicing fees must be paid from the 1 1/8% that Board is allowed to earn. Servicing fees are .375% of the mortgage principal balance. The Board does not always receive the full 1 1/8% or 1 1/2% spread. The spreads for the last several bond issues were as follows:

* 1995B1 - .8799%
* 1995B2 - .8167%
* 1996A - 1.125%
* 1997A1 - 1.39063%
* 1997A2 - 1.08842%
* 1998A - 1.10078%
* 1998B - 1.04678%
* 1999A - 1.11985%
* 2000A - 1.10302%

* 2000B – 1.11709%
* 2001A - 1.11898%
* 2002A - 1.12251%
* 2002B - 1.09666%
* 2003A1 - 1.21126%
* 2003A2 - .07883%
* 2003B1 - 1.45392%
* 2003B2 - .51062%
* 2003C - .83833%
* 2004A - .82319%
* 2004B - .49576%

*Operating expenses and servicer fees further reduce the amount of these earnings.
The 1 1/8% or 1 1/2% that the Board can earn is based on certain assumptions at the time the bond issue is structured. One of the assumptions is that the loans will prepay at 100% of the historical FHA prepayment rate. If the loans actually prepay faster, the Board will not earn the initial spread that was calculated. The Board only earns this spread if the loans are held for the amount of time that is originally estimated. If the loans prepay early, the money is invested and then is used to redeem bonds. When the mortgages pay off, the Board has lost the ability to earn the spread between the mortgage yield and bond yield. Historically, prepayments on the majority of the loans have been over 100%, and we expect this trend to continue.

The Board also charges a cancellation fee of 1/2 of 1% of the loan amount reserved. Approximately 5% of loans reserved are canceled. This amount is included in the spread that the Board can earn. These fees are capitalized and are amortized as income over the life of the loans, as required by generally accepted accounting principles. Extension fees and late fees are also, occasionally, charged. The majority of these fees are capitalized and amortized over the life of the loans. The extension fees are 1/4 of 1% of the loan amount and the late fees are 1/2 of 1% of the loan amount. The amortization of these fees results in an average of approximately $250,000 of income per year. These fees are deposited with the trustees and are used to originate new mortgages.

Multifamily Charges:

Multifamily Programs can earn 1 1/2% spread between the mortgage yield and the bond yield. On the last several issues, the Board did not receive the full 1 1/2% spread. The spreads for the last four bond issues are as follows:

* 1992A - 1.0677%
* 1996A - .826%
* 1998A - .28156572%
* 1999A - 1.013963%

(Servicing fees and operating expenses further reduce the amount of this spread.)

We have currently had one loan payoff and one loan looking at a payoff. It is always a possibility that loans will make prepayments but until that happens it is hard to predict this scenario. If these loans prepay, bonds will be redeemed with the prepayments, and the Board will no longer earn any spread on these loans. In the 1992A bond issue, the Board is currently using excess revenues to purchase loans at interest rates that are lower than the bond yield. This further reduces the amount of earnings in the Multifamily Program. Under the Multifamily Program, the board can charge a reservation fee, on new loans, of up to 1% of the principal balance. Normally, the Board charges less than this amount.

Low Income Housing Tax Credit Charges:

The Board receives $2.075 million dollars of tax credit allocation, annually. The Board charges 4 1/2% of the amount of tax credit reserved. In the next biennium, reservation fee income is estimated to be approximately $93,375 per year. The Board is also required to monitor the projects that receive tax credits to determine if the projects are in compliance with tax credit regulations. The Board charges $25 per unit for compliance fees. The Board has approximately 4,000 units. Approximately $100,000, annually, will be received during the biennium. Tax credit fees are charged to cover the operating expenses of the program.

Housing Revolving Loan Account Charges:

The 1999 Legislature established this fund to provide loans to projects providing affordable housing in Montana. Although the fund was established in 1999 it was not funded. The 2001 legislature added funding through a transfer of Section 8 reserve funds and an allocation of Temporary Assistance to Needy Families (TANF). The TANF funding is currently used to finance down payment and closing cost loans for homebuyers. The other funding is available for other types of housing loans that will typically need that last small piece of financing to make them feasible. The interest that will be charged on HRLA loan will range from 2% - 6%.

Reverse Annuity Mortgage Loans (RAM) Charges:

Under the RAM program, elderly homeowners can receive monthly payments, for 10 years, to assist them with their living expenses. The loans accrue interest at 5%. The principal and interest is not due until the borrower dies or sells their home. It is difficult to determine how much of the interest and principal will actually be received on these loans or when it will be received. These loans are not guaranteed or insured.

Increase in Mortgage Income:

The Board's mortgage income steadily increased from FY1999 to 2002 and leveled off in FY2003 because of significant prepayments. Part of the reason is because there are four Single Family bond issues (1995B, 1997A, 2003A & 2003B) that were structured to use loan prepayments and excess revenues to originate loans rather than to call bonds or pay debt service. These bond series have 40 year bonds rather than the typical 30 year bonds. These series do not have principal payments on the bonds for 10 years, only interest is due. During the first 10 years of each bond issues, mortgages will be originated with prepayments and the excess revenues. The 1995B-1 will begin paying principle in June 2006 however the Board is researching avenues to extend this requirement.

The Board has continued to issue bonds each year to originate new mortgages. During fiscal years 2002, 2003 & 2004, the Board issued bonds in the amounts of $89,180,000, $143,965,000 & $161,800,000, respectively. We anticipate mortgage revenue will continue to increase during the next biennium as the Board continues to originate loans with prepayments, excess revenues and bond proceeds.

Investment Income:

In fiscal year 2003, the Board earned approximately $11,955,945 on its investments. During the latter part of fiscal year 2000, the Board entered into a repurchase agreement on its Single Family II Indenture. The repurchase agreement is at 6.43% for 30 years and will help us predict investment income in the upcoming years.

NOTE: For Post 1980 Single Family issues and Post 1986 Multifamily issues, investment earnings cannot exceed the yield on the bonds.

Increase in Fair Market Value:

The increase in fair value is a requirement of GASB 31. It requires that all investments be valued at fair value. During 1998, the first year that GASB 31 was implemented, the Board recorded a gain of approximately $2.8 million. In FY2003 the amount was approximately $2.3 million. We anticipate an approximate decrease of $2.3 million in FY2004. The Board does not intend to sell the long-term investments. If they are sold, we will receive the value of the investment on the day of the sale. This amount could be substantially different from the market value at June 30th. We did not estimate any increases or decreases in the fair value for fiscal year 2005, 2006 or 2007. The market fluctuations are significant and it is impossible to estimate the value of the investments at any given time.

Board of Housing revenues (accounting entities 06030, 06031, 06078, and 06079) are primarily recorded in the following SABHRS revenue codes:

	FY 2004	%
512033	$ 312.38	0.001%
526062	$ 214,711.93	0.498%
530014	$ (2,230,747.82)	-5.179%
530025	$ 16,833.03	0.039%
538006	$ -	0.000%
538025	$ 18,607.70	0.043%
538040	$ 39,367.48	0.091%
538041	$ 36,135,142.23	83.888%
538042	$ 8,379,696.53	19.454%
538046	$ 4,924.53	0.011%
538402	$ -	0.000%
581141	$ 3,400.00	0.008%
581601	$ 241,675.00	0.561%
593401	$ 12,943.00	0.030%
599001	$ 238,507.85	0.554%
Totals:	$ 43,075,373.84	100.000%

Expense Description:

Operations & personal services expense:

Operations for the next biennium are anticipated to be approximately $5.6 million for FY 2006 and $6 million for FY 2007. The operating expenses include the following:

Servicer fees:	$2.8 million (FY 2006)	$3 million (FY 2007)
Operating expenses & personal services:	$2.8 million (FY 2006)	$3 million (FY 2007)

The operations of the Board include purchasing mortgage loans, receiving repayments and prepayments, investing funds, issuing and redeeming bonds. During fiscal year 2004, the Board purchased $153,813,245 in mortgages and received $180 million in mortgage repayments, prepayments and interest. The Board paid interest and principal on bonds of $193,454,965 and issued new bond proceeds in the amount of $161,800,000. This was done with a staff of 20 FTE.

Miscellaneous Operating expense:

Miscellaneous operating includes the interest expense on bonds. It also includes the periodic amortization of the cost of issuance expense. The costs associated with issuing the bonds are expensed over the life of the bonds, as required by generally accepted accounting principles.

During fiscal years 2002, 2003 & 2004, the Board issued bonds in the amounts of $89,180,000, $143,965,000 & $161,800,000, respectively. The issuance of new debt in FY 2004 has approximated maturities and redemptions on bonds. The Board anticipates an increase in debt service during the next biennium.

The major cost drivers within the Board of Housing are personal services, operating expenses, expenditures related to the periodic replacement of computer equipment. Additionally, over $38.685 million was disbursed from accounting entity 06030 in FY 2004 via an administrative appropriation for debt service requirements related to the Board's bonding activity.

FY 2004 base year expenditures for accounting entities 06030, 06031, 06078, and 06079 are as follows:

	FY 2004	%
FTE	20.00	
Personal Services	$ 828,467.29	2.016%
Operating Expenses	$ 3,662,585.30	8.915%
Debt Service	$ 36,594,057.01	89.069%
Totals:	$ 41,085,109.60	100.000%

There is little uncertainty in forecasting major cost drivers and for the purposes of this analysis it is assumed the Board's workload and customer level will remain constant.

Non-typical and one time only expenses, if any, are subtracted from proposed budgets. The Board of Housing is authorized 20.00 FTE and personal services expenditures include Board Member Per Diem.

Working Capital Discussion:

Collection of mortgage payments & purchase of loans:

Each month the Board receives funds from the financial institutions that service the Board's Single Family and Multifamily loans. The funds include the amount of principal, interest, less servicing fees (.375%, .125% and .10% of the principal balance) that are due on the Board's loans. The Board's trustees collect the money. Twice monthly, the Board purchases loans from new bond proceeds, prepayments or other revenues.

The Board receives tax credit reservations fees when the tax credits are approved. These fees are deposited with the state treasurer and are used to cover expenses of the program. Reservations fees on the Single Family and Multifamily Programs are deposited with the trustees when the approved loans are reserved. They are deposited in the program acquisition account and are used to originate new mortgages.

Payment of Bond P & I:

Principal and interest, on the Multifamily and Single Family Bond issues, is due on each February 1, April 1, June 1, August 1, October 1 and December 1. During fiscal year 2004, the Board paid $193,454,965 in principal and interest on the bonds.

This number includes scheduled principal and interest payments as well as bond redemptions from prepayments and excess reserves and other revenues. The amount of debt service paid will vary depending on the amount of prepayments received. Under the Single Family I and II Indentures, except for those series that were structured for recycling, each semiannual debt service date, the Board determines how many prepayments have been received. The Board uses the loan prepayments to redeem bonds in an amount equal to the prepayments received. The income cannot be used for any other purpose. Annually, the Board reviews any other revenues and excess reserves in the Single Family programs and those amounts are also used to redeem bonds. The Multifamily Program has received prepayments on two loans and bonds will be redeemed. In the future, there may be prepayments, and bonds will also be redeemed.

Investment of funds;

In the Single Family I and II Indentures, the Board invests the majority of prepayments and repayments of loans in repurchase agreements. The interest coming due on the agreements also coincides with a debt service date. In three of the series under the Single Family II Indenture, prepayments and any other revenues are used to originate loans that could not otherwise be originated under the tax laws. These two series do not have principal due on the bonds for the first 10 years of the bond issue. These funds are normally invested based on the anticipated loan purchase dates. Under the Single Family I Indenture, a portion of prepayments and repayments are used to originate loans that do not meet the tax laws. These funds are currently invested in a repurchase agreement and withdrawn, as the funds are needed for purchases.

The deposit of the initial bond proceeds, used for purchasing loans, is normally invested in a two-year, fixed rate, repurchase agreement. All debt service reserve funds and mortgage reserve funds that must be held as security for the bondholders are invested in long-term securities, repurchase agreements or guaranteed investment contracts. Under the Multifamily Program, the funds are invested to the next debt service date or to a loan purchase date.

Other Mortgage Purchases:
The Board purchases Reverse Annuity Mortgage (RAM). The RAM loans are not repaid until the borrower dies or sells their home. These amounts are assets of the Board and the interest is accrued monthly, but we may not receive the principal and interest repayments for many years.

The Board also purchases out of the Housing Revolving Loan Program. These loans can be due on sale or amortizing. These amounts are assets of the Board and the interest is accrued monthly.

Fund Equity and Reserved Fund Balance:

Net Assets/Restricted Net Assets;

As stated in the Board's financial statements, Note 1, Fund Accounting: Net Assets – Restricted for Bondholders represent bond program funds that are required to be used for program purposes as prescribed by individual bond indentures. The following are restrictions on the Restricted Net Assets: Special trust funds and accounts within the indenture are pledged as collateral for the bonds under the individual program indentures; Reserve requirements on cash and investments; Mortgage loans receivable are also pledged as security for holders of the bonds; Certain indentures require asset-liability coverage ratios be met as well as cash flow certificates be furnished for any significant change anticipated in the financial structure of an indenture.

The Trust Indentures entered into by the Board requires all mortgages, and all moneys and investments within the indentures are legally restricted to uses provided for in the indentures and fund balance associated with the indentures is legally required to be reserved for those uses.

In addition to the legal requirements mentioned above, the Board commits funds to various projects and programs throughout the year. The Board has set aside over $200 million of first mortgage funds for special programs, and originates approximately $20 million per year of new loans under this program (targeting income levels of approximately $20,000). As of the end of FY 2004, the Board had $37,946,710 in outstanding Recycled Mortgage Program commitments.

In the Multifamily area, the Board commits funds to projects around the state, with the intent to pool mortgages and issue bonds to fund mortgages and reimburse the Board where it has advanced funds on some of the projects. The Board has 29 active first mortgages with initial principle balances of $23,969,458. There are also 8 second position loans funded from a AHP grant awarded to the Board by the Federal Home Loan Bank of Seattle. The Board has 2 loans prepay and 2 loans foreclosed on.

In order to operate a more efficient Multifamily program, the Board was awarded a rating of A2 for its General Obligation on April 8, 1997. In order to obtain the A2 rating, the Board pledged that it will use any and all of the moneys, assets or revenues of the Board to back bonds issued using the General Obligation rating. All of the Board's bond issues, with the exception of the Single Family III through X (issued from 1988-1992) hold the Board's General Obligation pledge.

The fund balance within the Housing Trust Fund is legally required to be reserved for security to the single family programs by Resolution 92-0821-S1, the Fifth Supplemental Trust Indenture for its Single Family II Indenture and by Resolution 93-0624-S2.

The Board funds its RAM programs from the Housing Trust fund, because these are programs for which the Board can not issue bonds. As of the end of FY 2004, the Board has RAM loans with an outstanding principal balance and interest of $904,177. Outstanding commitments from the Housing Trust Fund as of FY 2004 were $1,441,763 for RAM.

The Board's budget monies (those projected to be needed for the fiscal year's operations) are drawn down from the indentures at the beginning of the fiscal year. These funds are legally pledged to the trust indentures from which they were drawn and any associated fund balance is reserved for the program from which the budgeted funds were withdrawn.

Management Objectives Regarding Fund Balance;

The major component of the Board's Fund Balance (Retained Earnings) is its single-family program. The Board has been recycling repayments and prepayments of mortgages for several years. The Board has committed these funds to special programs, at rates that are in many cases below the average coupon on the bonds. The average income on the special programs is less than $24,000, whereas the average income on the Board's regular bond programs is about

$35,000. The Board intends to continue these special programs as they serve Montana citizens the Board would not otherwise be able to serve.

Net income over and above bond debt service, operating costs, and servicing fees, is used to write down the rates on special programs or to fund programs such as the RAM Program for elderly. These programs cannot be funded from direct bond proceeds, as there is no repayment guarantee. In the Multifamily area, the Board intends to continue to leverage its multifamily funds into new multifamily loans through the revolving pool so that loans can be completed in a timely and efficient manner.

The Board is reviewed at the time of each bond issue by two rating agencies: Standard & Poor's, and Moody's Investor Services. In order to meet the cash flow tests, the Board must have sufficient assets, earnings, and liquidity, to meet all bond interest and principal expenses, as well as pay operating expenses. The Board just received an Aa2 from Moody's and a AA+ from Standard & Poor’s on its largest indenture. The Board's rating reflects the rates the Board gets on its bonds, which is reflected in the mortgage rates passed on to first time home buyers in Montana. In 1990, the Board purchased 1 in 10 of the mortgages. In 2002, the Board purchased 1 in 4 of these mortgages. The Board's continuous funding (which was a goal of current management set in 1994) and steady, low interest rates, as well as the Board's special programs, have contributed to this increase. In addition the increase in housing costs in Montana has made the need for lower interest rate financing even more profound.

Rate Explanation:

The Board recovers its costs from charging application and compliance fees for the Low Income Tax Credit Program and from charging a spread on our loan programs. The Board draws funds for its budget from the amounts available within the Indentures. The amount of the approved budget, less any cash on hand, is withdrawn from the Indenture and is allocated among the various Indentures. Any income the Board earns is used to fund special programs that meet the needs of Montana families that are not being met by our regular programs. These funds are pledged to the bondholders.